

**DEPARTMENT OF FINANCE AND ADMINISTRATION POLICY 22**  
**Subrecipient Contract Monitoring**  
(Revised 7/1/04)

**Introduction**

1. This policy statement 22 establishes subrecipient contract monitoring requirements for the State of Tennessee. The policy statement requires the monitoring of contracts awarded to subrecipients that include state and/or federal funds from state departments, agencies, and commissions (hereafter, referred to as state agency).

**Applicability and Effective Date**

2. This policy statement is applicable to all state agencies that award state and/or federal funds to subrecipients, as defined in paragraph 9, excluding colleges and universities.

The requirements of this policy are effective for the fiscal years beginning after June 30, 2004, and any grants/contracts issued which relate to such fiscal years.

**Purpose of the Policy**

3. The purpose of the policy is to define subrecipient contract monitoring, identify the required core monitoring areas and establish uniform subrecipient contract monitoring requirements to ensure consistent monitoring of subrecipient contracts by various state agencies that award state and/or federal funds to subrecipients. State agencies affected by the policy must perform all required subrecipient contract monitoring activities to ensure compliance with the policy.

**Basis for Authority**

4. The Commissioner of the Department of Finance and Administration, in consultation with the Comptroller of the Treasury, is required to establish guidelines for the evaluation by agencies of their systems of internal control as provided by *Tennessee Code Annotated*, Title 9, Chapter 18.
5. In addition, Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*, requires the state to monitor activities of subrecipients and to ensure compliance with program and administrative requirements.

**Implementation Guidance**

6. The June 2004 version of the *Tennessee Subrecipient Monitoring Manual*, issued by the Department of Finance and Administration, provides guidance for monitoring activities in accordance with this policy.

**Definition of Monitoring**

7. Monitoring is the review process used to determine a subrecipient's compliance with the requirements of a state and/or federal program, applicable laws and regulations, and stated results and outcomes. Monitoring also includes the review of internal controls to determine if

the financial management and the accounting system are adequate to account for program funds in accordance with state and/or federal requirements. Monitoring should result in the identification of areas of non-compliance with the expectation that corrective action will be taken to ensure compliance.

### **Monitoring Staff**

8. To the extent possible, there should be a separation of duties between monitoring staff and program operations to allow for independence and objectivity. Possible conflicts of interest should be disclosed.

### **Definition of Subrecipients**

9. A subrecipient is a non-federal entity that expends state and/or federal funds received from the state to carry out a state and/or federal program. Subrecipients would also include state colleges and universities if they receive federal funds from a state department or agency.

A vendor is a dealer, distributor, merchant, or other seller providing goods or services that are required for the conduct of a Federal program. These goods or services may be for an organization's own use or for the use of beneficiaries of the Federal program.

There may be unusual circumstances or exceptions to the characteristics of subrecipients and vendors. In making the determination of whether a subrecipient or vendor relationship exists, the substance of the relationship is more important than the form of the agreement. It is not expected that all subrecipient characteristics will be present. Judgment should be used in determining whether a contract represents a subrecipient or a vendor relationship. If the contractual relationship with the state meets the vendor criteria, then the state agency must ensure that the procurement, receipt, and payment for goods and services comply with laws, regulations, and the provisions of the contract.

To distinguish a subrecipient from a vendor, use the characteristics below from OMB Circular A-133, Section .210.

<b>Subrecipient Characteristics</b>	<b>Vendor Characteristics</b>
Determines who is eligible to receive state and/or federal financial assistance available through the program administered	Provides the goods and services to many different purchasers
Has its performance measured against whether the objectives of the state and /or federal program are met	Provides goods and services within normal business operations
Has responsibility for programmatic decision making	Operates in a competitive environment
Has responsibility for adherence to applicable state and/or federal program compliance requirements	Provides goods or services that are ancillary to the operation of the state and/or federal program
Uses state and/or federal funds to carry out a program of the state as compared to providing goods or services for a program of the state	Is not subject to compliance requirements of the state and/or federal program

10. Any entity meeting the subrecipient criteria will be subject to subrecipient contract monitoring including private non-profit entities, for-profit entities, governmental entities, and state and local governments.

### **Subrecipient Contract Monitoring Plan - General Rule**

11. All state agencies affected by this policy must develop and submit an annual monitoring plan, for review and approval, to the Department of Finance and Administration, Division of Resource Development and Support, by October 1<sup>st</sup> of each year, beginning in 2004.
12. The monitoring plan is a summary of the agency's planned monitoring activities for the current annual monitoring cycle and must include the following components:
  - Total subrecipient contract population
  - Subrecipient contracts to be monitored during the current monitoring cycle
  - Identification of agency monitoring cycle (i.e. state fiscal year, federal fiscal year)
  - Sample monitoring guide/s to be utilized for each state and/or federal program
  - Full-time equivalents and personnel classifications for all staff dedicated to monitoring activities
  - A program description of each state and/or federal program being monitored
  - Risk assignment for each subrecipient and its related contract/s
  - Explanation of criteria used to assign risk to subrecipients and their related contract/s
  - Summary of findings from previous monitoring year
  - Explanation of the agency's corrective action process

Any changes to the monitoring plan following approval by F&A shall be documented by the agency and maintained with their approved plan. Changes to the population of contracts to be monitored should be particularly well documented with an explanation accompanying the changes made.

### **State Monitoring Requirements**

13. All state agencies affected by the policy shall utilize the following approach for the selection of subrecipient contracts to be monitored, unless specifically prohibited by state and/or federal program guidelines.
  - Subrecipient contracts associated with programs that have federally mandated monitoring requirements, which dictate the *frequency* of monitoring, should be monitored *as often as federally required*. Therefore, these contracts should not be included in the 1/3 and 2/3 calculations, described below, used to identify the population of contracts to be monitored during a given year.

While the state's criteria for choosing the population of contracts to be monitored each year will not apply to contracts associated with programs that have federal frequency requirements, the core monitoring areas (discussed in paragraph 14) covered during these reviews should not differ. All applicable core monitoring areas must be addressed for every review conducted.

- When selecting the population of contracts to be monitored each year two main criteria must be met:

- A. Affected agencies must annually monitor a **minimum** of 1/3 of the total number of all subrecipient contracts executed by their agency (in addition to those chosen to meet the federal monitoring frequency requirements).

**AND**

- B. The aggregate current year maximum liability value of the contracts selected **must be equal to or greater than** 2/3 of the aggregate current year maximum liability value of the agency's entire subrecipient grant population (this value should not take into account contracts chosen to meet federal monitoring frequency requirements).

Refer to the *Tennessee Subrecipient Monitoring Manual* for instruction on addressing contracts that do not have a maximum liability value assigned to them.

- Risk should be assigned to all subrecipients. While the scope of a review may vary based on the perceived risk to the state agency it must include, at a minimum, the program specific monitoring requirements as well as the applicable core monitoring areas outlined in paragraph 14.
- When choosing the population of contracts to be monitored, consideration should be given to contracts which:
  1. based on their state agency assigned risk assessment, pose a greater risk to the state (programmatically and/or financially)
  2. have not recently been monitored
  3. have prior review findings that indicate serious deficiencies
- Refer to the *Tennessee Subrecipient Monitoring Manual* for an example/visual representation of the process described in paragraph 13.

**Core Monitoring Areas**

14. In addition to state and/or federal program specific monitoring requirements, all monitoring activities undertaken by any state agency should address the following areas:
- A. All requirements of Title VI of the Civil Rights Act of 1964, as defined in the Title VI Compliance Commission Advisory Memorandum No. 3 issued April 14, 2004. A copy of this memo has been included in the *Tennessee Subrecipient Monitoring Manual*.

**AND**

- B. The applicable core monitoring areas, as defined by the OMB Circular No. A-133 Compliance Supplement. Currently, these core areas include: activities allowed or unallowed; allowable costs/cost principles; cash management; Davis-Bacon Act; eligibility; equipment and real property management; matching, level of effort, and earmarking; period of availability of funds; procurement, suspension and debarment; program income; real property acquisition and relocation assistance; reporting; and special tests and provisions.

Should the OMB Circular No. A-133 Compliance Supplement core areas change agencies must ensure that the core areas covered during monitoring activities mirror the most recent OMB A-133 Compliance Supplement.

### **Requirements for Reporting**

15. State agencies shall issue reports summarizing any findings and/or observations identified during monitoring reviews within 30 business days after the completion of all fieldwork. Reports shall be distributed to the subrecipient entity, as well as the Comptroller of the Treasury, Division of State Audit, and a copy retained by the state agency that conducted the monitoring review.

Upon receipt of the monitoring report, the subrecipient shall prepare a corrective action plan outlining the steps that will be taken to correct findings, if any, identified in the monitoring report. The corrective action plan shall provide the name/s of the contact person/s responsible for corrective action, the corrective action planned, and the anticipated completion date. If the subrecipient does not agree with the findings or believes corrective action is not required, then the corrective action plan shall include an explanation and specific reasons.

The corrective action plan shall be submitted to the state agency for their review and approval. It is the responsibility of the state agency to notify the subrecipient, in a timely manner, concerning the approval or rejection of the corrective action plan. If a corrective action plan is not approved, the state agency and the subrecipient shall work together to develop solutions for correcting the monitoring report findings.

### **Compliance Reviews**

16. Agency and department activities conducted, and records maintained, pursuant to this policy shall be subject to evaluation by the Department of Finance and Administration, the Comptroller of the Treasury, or their duly appointed representatives.